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Message Text

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ACTION EB-08

INFO OCT-01 NEA-10 ISO-00 AID-05 CIAE-00 COME-00
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E.O. 11652: GDS
TAGS: EFIN, ECON, EAGR, EAID, IMF, CE

SUBJ: IMF TEAM COMMENTS ON SRI LANKAN ECONOMIC PERFORMANCE

1. SUMMARY: INTERNATIONAL MONETARY FUND (IMF) OFFICIALS VISITN COLOMBO HAVE BEEN IMPRESSED BY THE ECONOMIC MEASURES TAKEN BY THE GOVERNMENT OF SRI LANKA (GSL) AND VERY PLEASED BY THE GSL'S APPARENT DETERMINATION TO FURTHER REDUCE SUBSIDIES. SRI LANKA'S BALANCE OF PAYMENTS AND BUDGETARY SITUATION ARE BETTER THAN EXPECTED. ANOTHER IMF TEAM WILL BE IN COLOMBO IN JUNE TO NEGOTIATE SRI LANKA'S ELIGIBILITY FOR FUND RESOURCES IN ADDITION TO THE CURRENT STAND-BY ARRANGEMENT; ADDITIONAL RESOURCES COULD AMOUT TO AS MUCH AS SDR 360 MILLION OVER A THREE YEAR PERIOD. SRI LANKA'S HIGH STANDING WITH THE IMF CONTRASTS SHARPLY WITH THE MORE CAUTIOUS VIEW OF THE WORLD BANK. END SUMMARY.

2. A TEAM OF IMF EXPERTS HAS JUST COMPLETED A TWO-WEEK VISIT IN PREPARATION FOR FORMAL NEGOTIATIONS IN JUNE FOR POSSIBLE SRI LANKAN USE OF THE EXTENDED FUND FACILITY AND OTHER IMF RESOURCES. IN CONVERSATIONS WITH US, TEAM MEMBERS MADE THE FOLLOWING OBSERVATIONS ON THEIR FINDINGS:
-- THE FUND OFFICIALS ARE IMPRESSED WITH WHAT THE GSL HAS
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ACCOMPLISHED SINCE TAKING OFFICE (I.E., ELIMINATION OF RICE AND SUGAR RATIONS FOR HALF THE POPULATION, DEVALUATION, IMPORT AND EXCHANGE CONTROL LIBERATLIZATION, AND GREATER RELIANCE ON PRIVATE SECTOR INITIATIVE). DESPITE THE ON-MONTH DELAY IN IMPLEMENTING THE RATION CUT, THE PROCESS OF REVALIDATING THE RATION BOOKS WAS A DIFFICULT JOB WELL DONE. SOME 50,000 PEOPLE WERE INVOLVED IN REVIEWING THE INCOME LEVELS

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OF EVERYONE IN THE COUNTRY. MEMBERS OF PARLIAMENT WERE BROUGHT INTO THE EXERCISE, AND THE UNIED NATIONAL PARTY'S ORGANIZATION WAS MOBILIZED TO MAKE SURE THE REVALIDATION PROCESS WAS AS FAIR AS POSSIBLE.
-- A NUMBER OF ACTIONS ANNOUNCED IN THE NOVEMBER 15 BUDGET SPEECH WITH WHICH THE FUND WAS LESS THAN HAPPY, HAVE NOT BEEN IMPLEMENTED. ACCORDING TO ONE IMF OFFICIAL, HE WAS PRESENT WHEN PRESIDENT JAYEWARDENE ORDERED THAT NO LEGISLATION WAS TO BE INTRODUCED TO PLACE ANY LIMITS ON PRIVATE SECTOR SALARIES (THE BUDGET PROPOSED A RS. 3,500 ($230) CEILING ON MONTHLY SALARIES). ALSO, THE PROPOSED RS. 50 PER MONTH PAYMENT TO EACH UNEMPLOYED ADULT HAS NOT BEEN PAID AS YET AND MAY NEVER BE PAID.
-- THE FUND TEAM WAS EVEN MORE STUCK WITH WHAT THE GSL SAYS IT PLANS TO DO. FLOUR PRICES WILL BE INCREASE, PERHAPS BEFORE THE APRIL 14 SINHALA-TAMIL NEW YEAR. FROM THE PRESIDENT ON DOWN, SENIOR GSL OFFICIALS AVER THEY ARE DETERMINED TO EVEN-TUALLY DO AWAY WITH "ALL SUBSIDIES," FOOD, FERTILIZER, TRANS-PORTATION, ETC. WHILE THIS WILL NO DOUBT TAKE SEVERAL YEARS TO ACCOMPLISH, IF EVER, FUND OFFICIALS ARE CONVINCED THAT THE GSL INTEND TO MOVE AS QUICKLY AS THE DOMESTIC POLITICAL SITUATION WILL PERMIT.
-- ON THE CURRENT ECONOMIC SITUATION, THE IMF REPORTS THAT SRI LANKA RECORDED AN OVERALL BALANCE OF PAYMENTS SURPLUS IN 1977 AND THROUGH THE FIRST TWO MONTHS OF 1978. EXPORT EARN-INGS ARE HIGH, THE LEVEL OF IMPORTS IS RUNNING BELOW EXPEC-
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TATIONS, AND FOREIGN EXCHANGE RESERVES CONTINUE TO INCREASE. AFTER SO MANY YEARS OF RIGID IMPORT CONTROLS, THE PRIVATE SECTOR IS HAVING DIFFICULTY ADJUSTING TO ITS NEW FREEDOM. THE TARIFF COMMISSION ESTABLISHED TO MAKE CONTINUOUS ADJUST-MENTS IN DUTIES TO MEET LOCAL NEEDS IS WORKING WELL. SHORTLY AFTER THE IMPORT LIBERATLIZATION, WHEN LICENSING RESTRICTIONS WERE ELIMINATED IN FAVOR OF TARIFFS AS A METHOD BY CONTROLLING IMPORTS, A NUMBER OF DOMESTIC MANUFAC CQERS COMPLAINED THAT THEIR TARIFF PROTECTION WAS NOT SUFFICIENT TO ALLOW THEM TO SURVIVE.TECTION WAS NOT SUFFICIENT TO ALLOW THEM TO SURVIVE. AND THE COMMISSION ASKED MANUFACTURERS TO PRE-

SENT PROFIT AND LOSS STATEMENTS TO SUBSTANTIATE THEIR CLAIMS, MOST REQUESTS FOR HIGHER DUTIES WERE ALLEGEDLY DROPPED. FUND EXPERTS WERE TOLD THAT THE GSL BUDGET DEFICIT, ORIGINALLY ESTIMATED AT RS. 4,420 MILLION ($280 MILLION), MAY WELL BE ZERO THIS YEAR. REVENUES (PARTICULARLY FROM EXPORT TAXES) ARE BETTER THAN EXPECTED AND EXPENDITURES ARE RUNNING BELOW PROJECTIONS.
-- THE JUNE NEGOTIATIONS IN COLOMBO WILL DETERMINE SRI LANKA'S ELIGIBILITY FOR USE OF THE IMF'S EXTENDED FUND FACILITY AND, POSSIBLY, THE "WITTEVEEN FACILITY." IF APPROVED, SRI LANKA

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COULD DRAW UP TO SDR 360 MILLION (ROUGHLY $440 MILLION) OVER A THREE YEAR PERIOD BEGINNING IN JANUARY 1979 IN ADDITION TO THE SDR 93 MILLION AVAILABLE UNDER THE PRESENT ONE-YEAR STAND-BY ARRANGEMENT. BASED ON PRESENT PERFORMANCE, AND FUTURE PROMISES, FUND OFFICIALS DOUBT THAT SRI LANKA WOULD NEED TO DRAW THIS MUCH.

3. COMMENT: THE MEMBERS OF THE IMF TEAM ADMIT THAT PART OF THEIR PLEASURE REGARDING THE GSL MAY BE DUE TO THE TOTAL CON-TRAST WITH THEIR EXPERIENCES IN DEALING WITH THE PREVIOUS GOVERNMENT. THE TEAM MEMBERS HAD NOTHING BUT PRAISE FOR SENIOR GSL OFFICIALS INVOLVED IN FORMULATING ECONOMIC POLICY. THE GSL'S HIGH STANDING WITH THE FUND SHOULD HELP TO BOOST SRI LANKA'S CREDIT RATING WITH BILATERAL DONORS AND TO ENCOURAGE
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POTENTIAL FOREIGN INVESTORS. IT CONTRASTS SHARPLY WITH THE WORLD BANK'S MUCH MORE CAUTIOUS VIEW OF THE GSL'S ABILITY TO SOLVE ITS SECULAR PROBLEMS VIA MASSIVE DEVELOPMENT PROJECTS FUNDED BY FOREIGN DONORS.
WRIGGINS

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